CATO INSTITUTE
MEMORANDUM

FROM: Randal O'Toole
RE: Additional Commentary
DATE: September 15, 2020

Public-Private Partnership Utilization

While county toll road and mobility authorities are useful innovations, Texas continues to pass up another key funding innovation that has been used in many states: public-private partnerships. The merging of state and private capital for infrastructure development has raised hundreds of billions of dollars for new projects across the US without the need for new broad state taxes. In Virginia alone, a state whose population has continued to increase in recent years, somewhat like Texas', the state's P3 intuitive has brought in more than 16,000 new jobs, injected more than $3.5 billion into the economy, and achieved an average investment rate of 7:1. Meaning that for each dollar of taxpayer money invested in infrastructure, about seven are realized from private investment. On a per-capita basis, were Texas to follow the learned best-practices of P3 implementation in Virginia, this could result in well over $15 billion in private capital investment for the Texas economy.

There are typically two kinds of public-private partnerships: demand risk and availability payments. In a demand-risk partnership, the public grants a franchise to a private partner to build infrastructure and collect fees for the use of that infrastructure. The private partner takes 100 percent of the risk that the fees may not be sufficient to cover the cost. (Sometimes, the public has to promise not to build infrastructure that will directly compete with the private facility.) Generally, after several decades, the title of the infrastructure is transferred to the public. In an availability-payment partnership, the public contracts with the private partner to build and operate a facility and promises to pay the private partner a fixed sum over several decades to cover the costs. In this case, the public takes the risk that the facility will not generate enough income or value to make it worthwhile.

From the public point of view, the demand-risk partnership is superior. The advantage over only having the government build the facility is that the private partner can often do the work at a lower cost, especially if it has an incentive to try to earn a profit from user fees. Public agencies that use the availability-payment structure are often doing so mainly to evade debt limits: since the debt required for the project is on the private partner's books, the public agency can borrow more money for other things even though it is legally obligated to pay the private partner enough for it to repay the debt.